

**VERIFICATION OF
SELECTED LOANS
REFINANCED FROM
RESOURCES OF THE
HOUSING GUARANTY
PROGRAM**

**APRIL 1, 1998-
DECEMBER 31, 1998**

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VERIFICATION OF SELECTED LOANS REFINANCED FROM RESOURCES OF THE HOUSING GUARANTY PROGRAM

APRIL 1, 1998 TO DECEMBER 31, 1998

INTRODUCTION

Annual verification of loans refinanced by the Mortgage Fund from resources of the Housing Guaranty Program was based on the Implementation Agreement of November 9, 1992 between Poland and the United States of America concerning Assistance for the Housing Sector (with subsequent changes). This report is a renewal of the study "Verification of Selected Loans Refinanced by the Mortgage Fund from the Housing Guaranty Program" covering periods from April 1, 1997 to March 31, 1998. All comments on methodology included in the last report, and in particular those concerning verification objectives and methods, remain valid.

The current verification covered loans refinanced in the period between April 1 and December 31, 1998. In the above period the Mortgage Fund originated 118 loans from resources of the Housing Guaranty Program. Share of participating banks is shown in the table below:

Bank	Number of Refinanced Loans	Share in Pool of Loans Refinanced by the Mortgage Fund (in percent)
BISE Warsaw	102	86.44
Bank Pekao SA Random Branch	13	11.02
Bank Pekao SA II Łódź Branch	3	2.54

This year's verification was the last one, since, as reported by Bud-Bank, resources of the Housing Guaranty Program were fully utilized. *10 loans were selected at random for verification.* Loans were chosen among credit portfolios of bank branches in proportion to the share of a given unit in the total number of loans refinanced by the Mortgage Fund. The number of verified loans issued by the selected banks is as follows: BISE-six loans, Random Branch of Bank Pekao SA-two loans, II Łódź Branch of Bank Pekao SA-two loans.¹ Detailed data is included in Attachment A.

¹ A new bank, Bank Pekao S.A. became operational on January 1, 1999. It was established from four banks from Pekao S.A. Group, i.e., Bank Pekao S.A., Bank Depozytowo - Kredytowy S.A. in Lublin, Pomorski Bank Kredytowy S.A. in Szczecin and Powszechny Bank Gospodarczy in Łódź. The last bank participated in the Mortgage Fund Program. Its branches originated loans subject to verification.



Preparation of Visits in Banks

According to what was agreed between USAID and Bud-Bank, the mortgage fund employees had to inform selected participating banks about verification. Before visits in banks I received from Ms. Krystyna Dąbrowska, Director of the Construction and Mortgage Loan Department, a letter with basic information about selected banks, names and telephone numbers of people I could contact and agreed dates of visits. The following persons were indicated as responsible for arranging my visits in individual banks:

- Ms. Luiza Gołaszewska, Deputy Director – BISE Warsaw
- Ms. Krystyna Lipska, Senior Manager – Radom Branch of Bank Pekao SA
- Ms. Iwona Stolańska, Section Manager – II Łódź Branch of Bank Pekao SA

Preparation of site visits was good, both on the Bud-Bank side and Participating Banks side. All the above mentioned people provided me with necessary support.

Site visits in Participating Banks took place between June 24, 1999 and July 5, 1999: I visited Random Branch of Bank Pekao SA on June 24, BISE Warsaw on June 30 – July 1, and II Łódź Branch of Bank Pekao SA on July 5.

Review of Credit Documents

I had no reservation to credit documentation made available to me in the banks.

All comments made in the last report on differences in maintaining credit histories in different banks are valid. However, those differences do not affect merits of credit data.

It is almost a rule that before loan origination borrowers deliver all documents requested by the bank, but once the loan is made they frequently do not submit current tax returns or insurance policies. It resulted from conversation with employees that banks do not insist on updating documents provided borrowers make regular payments.

It is not quite clear how property value is estimated in the underwriting process. In particular it applies to two different situations. First, when property sale agreement is in foreign currency, if a Złoty exchange rate fluctuates during the underwriting process, the property and requested loan amount are frequently revalued. Different issues occur in case of single family house construction or when the property is purchased from a developer. Quite often final project costs are higher than planned, and project completion deadline is not accomplished. This, in turn, impacts value of the property.

The above shortcomings do not diminish positive opinion on credit documentation; they merely indicate difficulties encountered in the underwriting process.

There are no reservations to usable areas shown in credit documentation. As a reminder, Annex number 5 to the Implementation Agreement enforced on June 9, 1998, specifies maximum area of a single family house qualified as "Eligible Expenditures" as 280 square meters; all loans for properties over 100 square meters were refinanced after that date.

On-site Inspection of Projects Financed from Resources of the Housing Guaranty Program

After consultation with USAID, taking into consideration limited time for site visits in banks and long distance between bank and location of financed investment, I visited eight of ten selected for verification investment projects. I personally met one borrower. Bank officers assured me they tried to contact me with their customers and make appointments, but my visit took place in their working hours and they could not make it. Therefore I inspected seven properties only from outside.

For seven projects there were no noticeable inconsistencies between actual condition and that shown in credit documentation.

In two cases of loans for purchase of a single family houses: loan 0421.03 originated by BISE in Warsaw and loan 0433.01 originated by II Łódź Branch of Bank Pekao SA borrowers, having taken the loan and bought the house, started rehabilitation of purchased buildings; however the works were not funded from loans under verification.

There are serious reservations to loan No. 0409.01. In response to my inquiry about property area, the borrower reported it was approximately 400 square meters (I did not specify if I needed usable area). Moreover, credited property is not a primary dwelling of the borrower. He informed about it in *Mortgage Application Form BJ – 12/98*. Furthermore I discovered the whole property is currently in commercial, not in residential, use. *In my opinion such use breaches provisions of the Implementation Agreement.*

Interviews with Employees of Banks Originating Loans from the Mortgage Fund

During site visits, I had an opportunity to conduct several conversations on housing finance.

Only BISE experienced increase of amount of residential loans. In other banks credit action was considerably inhibited. In Random Branch of Bank Pekao SA I was



told they issued only several credits last months. In II Łódź Branch of Bank Pekao S.A. the official told me the best year was 1996, since then credit action has been decreasing. However all banks expect higher interest in residential loans in connection with plans to remove construction tax relief in 2000.

BISE has an interesting practice of property valuation. If a large number of customers of a certain developer, constructing a housing complex, use bank services the bank develops a so-called "model valuation report". Based on this report individual properties are estimated. Such procedure, in the opinion of a bank officer, reflects actual property value and releases customers from costs of individual appraisal.

BISE together with "G-12" banks is preparing to start a mortgage bank. In the opinion of bank officers the Mortgage Fund Program allowed the bank to gain know-how, necessary knowledge and expertise in origination of residential loans.

Comparison of Data Submitted from Bud-Bank to USAID and Data Existing in Participating Banks

Data on loans refinanced from resources of the Housing Guaranty Program submitted by Bud-Bank include the following inconsistencies as compared to data from documentation of Participating Banks:

- Loan number 0365.02. In USAID data loan amount, both in Bud-Bank and Participating Bank is 59,000, refinanced loan disbursement date is April 7, 1998. In BISE the loan amount is 53,000 (100 percent refinanced) and date of transfer from Bud-Bank is September 10, 1998. There is a refinance loan for BISE in the amount of 53,000 made on September 10, 1998, but this is loan number 0410.04 (sequence number in the USAID list 345).
- Loan numbers 0364.06 and 0409.01 are construction loans converted into mortgage loans.
- Loan number 0421.03 was repaid on May 13, 1999.

Apart from those exception Bud-Bank information is no different from data in participating banks.

Recommendations

- Have Bud-Bank explain actual usable area and uses of the property from loan number 0409.01.
- Get from Bud-Bank reasons of inconsistencies between data given to USAID and data on loan number 0365.02 verified this year.

- Conduct research regarding impact of the Program on development of housing finance in Poland. Such study could include results of strengths and weaknesses of the Program as perceived by the banks, as well as analysis of data existing in Bud-Bank and USAID on refinanced loan (e.g., average loan amount, structure analysis including amount, purpose, share of individual banks in total pool, etc.). Such research could be useful when designing similar programs in other countries.

ATTACHMENT A

Verification of Selected Loans Refinanced by the Mortgage Fund from Resources of the Housing Guaranty Program (Data according to information in Participating Banks)

Sequence Number*	Loan Number**	Bank	Purpose	Property Usable Area (square meters)	Purchase Price (Property Value) (Złoty)	Loan Amount (Złoty)	Gross Monthly Income (Złoty)	First Payment (Złoty)
271***	0369.01	Bank Pekao SA Radom Branch	Purchase of a unit in a multifamily building (primary market)	72.50	66614.08	30000 (refin. 15000)	2546.84	331.09
273	0365.02	BISE Warsaw	Purchase of a unit in a multifamily building (primary market)	55.90	107382	53000 (refin. 53000)	5000	600
288***	0364.06	BISE Warsaw	Construction of a single family house	93.46	84114	43979.50 (refin. 43979.50)	2729	490
307	0390.04	BISE Warsaw	Purchase of a unit in a multifamily building (secondary market)	72.46	275000	160000 (refin. 160000)	16287	2500
322	0400.05	BISE Warsaw	Construction of a single family house	163.52	255000	85000 (refin. 85000)	11000	1600
341	0409.01	Bank Pekao SA Radom Branch	Construction of a single family house	259.01	300200	75988.65 (refin. 37994.33)	4776.17	911.86
353	0410.12	BISE Warsaw	Purchase of a unit in a multifamily building (primary market)	49.30	96106	40000 (refin. 12314.72)	2150	440
373	0421.03	BISE Warsaw	Purchase of a single family house (secondary market)	179.10	450000	270000 (refin. 270000)	18000	3500
380	0433.01	Bank Pekao SA II Łódź Branch	Purchase of a single family house (secondary market)	204.20	110000	80000 (refin. 72000)	4000	1000
387	0451.01	Bank Pekao SA II Łódź Branch	Purchase of a unit in a multifamily building (secondary market)	51.92	48500	36375 (refin. 32737.50)	2729.92	545.98

* Sequence number on a summary loan list prepared by Bud-Bank.

** The following format is used:

XXX – loan number

XXX.YY – pool number loan number within a packet

*** Loan with no on-site inspection of property.